(13)

No. 92-1370

Supreme Court, U.S.
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In The

Supreme Court of the United States

October Term, 1993

IN RE: BFP, a Partnership,

Debtor.

BFP, a Partnership,

Petitioner,

vs.

IMPERIAL SAVINGS & LOAN ASSOCIATION; PAUL OSBORNE; WILLIAM LITTLE; DENNIS ROY; ARTHUR RITZ; JOSE CRUZ; RICHARD MARCZ,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF FOR RESPONDENTS PAUL OSBORNE, WILLIAM LITTLE, DENNIS ROY, ARTHUR RITZ, JOSE CRUZ AND RICHARD MARCZ

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QUESTION PRESENTED FOR REVIEW
(RULE 14.1(a))

Respondents believe that the only proper question for review is:

Did the United States Court of Appeals for the Ninth Circuit err in concluding that "the price received at a noncollusive, regularly conducted foreclosure sale establishes irrebuttaly reasonably equivalent value under 11 U.S.C. § 548(a)(2)(A)"?

LIST OF ALL PARTIES
(RULE 24.1(b))

Petitioner:

BFP, a Partnership,

Respondents:

Paul Osborne; William Little; Dennis Roy; Arthur Ritz; Jose Cruz; and Richard Marcz.

Respondent:

Resolution Trust Corporation as Receiver of Imperial Federal Savings Association.

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OPINIONS BELOW

In Re BFP, 974 F.2d 1144 (CA9 1992) (*See* Appendix to Amended Petition herein, p. 1). *In Re BFP*, 132 B.R. 748 (9th Cir. BAP 1991) (*See* Appendix to Amended Petition, herein, p. 49).

STATUTE INVOLVED

The only real statute involved in the decision of the Ninth Circuit Court of Appeals, and pertinently involved herein, is: 11 U.S.C. § 548(a)(2)(A). (*See* Appendix to Amended Petition, p. 69-70).

STATEMENT OF THE CASE

Petitioner has omitted several important substantive and procedural facts from its statement.

Petitioner was first a debtor in a Chapter 11 bankruptcy case (involuntary) on December 31, 1988 (Joint Appendix ("J.A."), pp. 23-25).

Imperial Federal Savings Association ("Imperial") (now represented herein by Respondent The Resolution Trust Corporation) ("RTC") held the most senior deed of trust on Petitioner's real property (Petitioner's Brief, p. 10). Because Petitioner had defaulted on its deed of trust payments, Imperial requested, and obtained, relief from the automatic stay, and permission, from the United States Bankruptcy Court to proceed with its pending non-judicial foreclosure and a trustee's (foreclosure) sale (J.A. p. 23 and 25).

Then, prior to formal entry of an order on Imperial's behalf, Petitioner voluntarily requested an order dismissing the Chapter 11 bankruptcy case. The order was entered, and the bankruptcy case dismissed, on June 14, 1989 (J.A. p. 24).

On July 12, 1989 — almost one month after the first bankruptcy case was dismissed, and over 3 1/2 months before the instant bankruptcy case was commenced — the real property was

sold by Imperial at a trustee's (foreclosure) sale.[1] Respondents Paul Osborne, et al., ("Respondents") were the third-party purchasers, paying $433,600 cash. At the time of the sale, the amount owed to Imperial was only $421,815.72 (J.A. pp. 232-236). The surplus proceeds were made available to the junior trust deed holders, whose $200,000+ junior deed of trust was extinguished by Imperial's foreclosure sale. *See* Calif. Civil Code § 2924k(a)(3).

A Trustee's Deed Upon Sale was executed and delivered on July 18, 1989, at which time title to the property became vested in Respondents (J.A. p. 235). *See* Calif. Civil Code §§ 1091, 1053, 1054. On July 21, 1989, the Trustee's Deed was recorded, pursuant to California law, with the official records of Orange County.

Two state court actions were then filed, by Petitioner and others, challenging the trustee's (foreclosure) sale (J.A. pp. 140-170). The first action was voluntarily dismissed by Petitioner and others. On October 25, 1989, two weeks after Respondents filed a demurrer challenging the sufficiency of Petitioner's complaint in the other action — and only 2 days before the hearing on Respondents' demurrer (J.A. pp. 175-201) — Petitioner filed this, its second, Chapter 11 bankruptcy case (J.A. p. 26).

On or about November 24, 1989, Petitioner filed its adversary

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1. Although Petitioner, again, refers to facts regarding "notice" (*see* Petitioner's Brief, pp. 13-14), Petitioner's adversary complaint did not seek to have the trustee's (foreclosure) sale set aside based on any lack thereof. Petitioner's adversary complaint did not allege any failure to comply with the strict notice requirements of California statutes. Petitioner expressly admitted to the Bankruptcy Court that it could not allege or prove any failure to comply with any requirement mandated by the comprehensive California statutes governing foreclosures. Petitioner received all the notice(s) required by law. Even if it had not, the foreclosure sale could not have been set aside as to Respondents pursuant to well-settled California law. *See* Point VII *infra*.

complaint and challenged the trustee's sale, and commenced the proceedings directly below (J.A., pp. 2-5, 41-62).

On December 14, 1989, the United States Bankruptcy Court vacated the automatic stay in Petitioner's Chapter 11 case "for all purposes" as to Respondents.[2] (J.A. pp. 102-104).

On March 6, 1990, after Petitioner admitted that it could not prove any non-compliance with California foreclosure statutes, the United States Bankruptcy Court, on Respondents' motion pursuant to Rule 12(b)(6) F.R.C.P. and Federal Bankruptcy Rule 7012(b), dismissed Petitioner's complaint as to Respondents (Appendix to Petitioner's Amended Petition, pp. 28-32). That dismissal was subsequently affirmed by both the United States District Court for the Central District of California and the Court of Appeals for the Ninth Circuit (*In re BFP,* 974 F.2d 1144 (CA9 1992) "Ninth Circuit's decision below"). (Appendix to Petitioner's Amended Petition, pp. 41-43, 1-23) (Petitioner's complaint against Imperial proceeded to a summary judgment in Imperial's favor. That judgment was subsequently affirmed by both the United States Bankruptcy Appellate Panel for the Ninth Circuit (*In re BFP,* 132 B.R. 748 (9th Cir. BAP 1991) and the Court of Appeals for the Ninth Circuit (*In Re BFP,* (9th Cir. 1992), *supra).* Pursuant to an order filed on November 17, 1992, Petitioner's petition to the Ninth Circuit for rehearing was denied, and its suggestion for rehearing *en banc* was rejected. No active circuit judge requested a

2. While Petitioner refers to a January 1990 resale of the property (*see* Petitioner's Brief, p. 11, fn. 1), no evidence of any resale or the deed referred to was *ever* presented to the Bankruptcy Court or District Court below, nor properly presented to the Court of Appeals ("J.A." pp. 1-10). Indeed, as Petitioner only sought to recover the property (J.A. pp. 61-62) and never sought relief pursuant to 11 U.S.C. § 550 (J.A. pp. 41-62), this proceeding is moot. *Heitmuller v. Stokes,* 256 U.S. 359, 361-62, 41 S. Ct. 522, 65 L. Ed. 990 (1921); *In re Mann,* 907 F.2d 923, 926 (CA9 1990); *In re Combined Metals Reduction Co.,* 557 F.2d 179, 190-91 (CA9 1977).

vote for a hearing *en banc* (Appendix to Petitioner's Amended Petition, pp. 26-27).

SUMMARY OF ARGUMENT

The plain meaning of the statutory phrase, "reasonable equivalent value", should be applied. As Respondents paid such value, Petitioner's request herein must therefor be denied.

The intent of Congress to interpret the term "reasonable equivalent value" contrary to pre-Bankruptcy Code and state practice is not evident, explicit or clear. There is no reason why the laws of the states which do not directly conflict with 11 U.S.C. § 548(a)(2)(A) cannot remain valid and enforceable. Significantly, Congress has failed to amend 11 U.S.C. § 548(a)(2)(A), or the United States Bankruptcy Code, to prohibit courts from reaching the same conclusion as the Court of Appeals for the Ninth Circuit reached.

The Ninth Circuit's decision below is in conformity with Bankruptcy Code provisions, and Congress' intentions, as to secured debt.

It is indisputable that an interest in real property, or a deed of trust, or the mechanics of a foreclosure and foreclosure sale must all be determined, even in a bankruptcy context, according to the laws of the various states. It is proper for a federal bankruptcy statute to be interpreted and applied so as to achieve harmony with the laws of a particular state or states. Indeed, such harmonization is essential and required for the orderly administration of justice.

Contrary to Petitioner's argument, the foreclosure sale could not be set aside as to Respondents due to any defect in notice, because Respondents were only third-party innocent purchasers. Indeed, 11 U.S.C. § 548(c) precludes any set aside as to Respondents.

ARGUMENT

I.

THE PLAIN LANGUAGE OF 11 U.S.C. § 548(a)(2)(A) DEFEATS PETITIONER'S CLAIM.

The starting point in statutory interpretation is the language of the statute itself. *United States v. James*, 478 U.S. 597, 604, 106 S. Ct. 3116, 92 L. Ed. 2d 483 (1986).

The statutory provision asserted by Petitioner's complaint, and applied by the courts below, is 11 U.S.C. § 548(a)(2)(A). The pertinent provisions of that section of the Bankruptcy Code allow a voluntary or involuntary pre-bankruptcy transfer of the debtor's property to be avoided if the debtor "received less than a reasonably equivalent value in exchange for such transfer."

Petitioner contended in its complaint below against Respondents that it had received less than the reasonably equivalent value from the foreclosure sale of its property. In looking at the plain language of § 548(a)(2)(A), however, it is clear that the price paid by Respondents at the sale ($433,600 cash, *see* J.A. pp. 232-235) satisfied the value requirements.

The statutory words are easily defined.

"Reasonably", qualifying "equivalent" means "in a reasonable manner; in conformity to the dictates of reason". (Webster's Dictionary, 2d ed. 1979).

"Equivalent" means that the consideration paid must be equal to the property transferred or the debt involved. *Kass v. Doyle*, 275 F.2d 258, 260 (CA2 1960); *In re Venie*, 80 F.S. 250, 256 (W.D. Mo. 1948); 4 Moore & King, *Collier On Bankruptcy* (15th ed. 1992)

¶ 548-09, p. 548-108.1; *see also, Central Nat. Bank v. Bell*, 5 Cal. 2d 324, 328 (1936) — according to California law the price paid at a foreclosure sale is deemed equivalent to the value of the property sold. "Reasonably equivalent" therefor requires an equivalent value which is reasonable under the circumstances. *Mellon Bank N.A. v. Metro Communications, Inc.*, 945 F.2d 635, 647 (CA3 1991); *In re Minnesota Utility Contracting, Inc.*, 110 B.R. 414, 420 (D. Minn. 1990) — reasonable equivalent value requires that the debtor receive a concrete benefit, like the discharge of a debt.

Herein, the purchase price paid by Respondents was in excess of Petitioner's debt to Imperial (J.A. p. 232; Petitioner's Brief, p. 10) and, under the circumstances of the foreclosure sale, was reasonable and equivalent.

"Value" means property or satisfaction of an antecedent debt. 11 U.S.C. § 548(d)(2)(A). "Value" also includes the payment of cash or other consideration. *Mayors v. Comm'r of IRS*, 785 F.2d 757, 761 (CA9 1986); *Kass v. Doyle, supra*, 275 F.2d at 260; *In re Venie, supra*, 80 F.S. at 256; *see* Calif. Civil Code § 1605. Herein, Respondents paid $433,600 in cash.

Respondents paid "value" for the property and, under the circumstances at the time of the sale and because their payment fully paid off the antecedent debt Petitioner owed to Imperial, that value was "reasonably equivalent" as required.

It is well-settled that there is a "strong presumption" that Congress' intent is fully expressed by the plain language in a statute. Herein, Petitioner has failed to demonstrate that Congress intended to go beyond the plain language in § 548(a)(2)(A). As this Court noted in *Ardestani v. I.N.S.*, __ U.S. __, 112 S. Ct. 515, 520, __ L. Ed. 2d __ (1992):

> The "strong presumption" that the plain

> language of the statute expresses Congressional intent is rebutted only in "rare and exceptional circumstances", *Rubin v. United States*, 449 U.S. 424, 430, 101 S. Ct. 698, 701, 66 L. Ed. 2d 633 (1981), when a contrary legislative intent is clearly expressed. (Citations omitted.) In this case, legislative history cannot overcome the strong presumption "that the legislative purpose is expressed by the ordinary meaning of the words used." *American Tobacco Co. v. Patterson*, 456 U.S. 63, 68, 102 S. Ct. 1534, 1537, 71 L. Ed. 2d 748 (1982).

See also, United States v. Ron Pair Enterprises, Inc., 489 U.S. 235, 109 S. Ct. 1026, 1031, __ L. Ed. 2d __ (1989).

This Court should apply the plain language of § 548(a)(2)(A) to the facts below and deny Petitioner's request herein. Petitioner has failed to present any legislative history showing Congress' contrary intent. Respondents clearly paid "reasonably equivalent value".

II.

THE PLAIN LANGUAGE OF 11 U.S.C. § 548(a)(2)(A), AND CONGRESSIONAL INTENT, DO NOT REQUIRE PETITIONER TO RECEIVE "MARKET VALUE".

Petitioner's position herein and below was that the purchase price paid by Respondent was less than the fair market value or "worth" of the property (Petitioner's Brief, pp. 10-11, 21; J.A. pp. 59-60; *see* Respondents' Court of Appeal Opening Brief, pp. 8-9).

Section 548(a)(2)(A) does not, however, refer at all to market value or worth. Section 548(d)(2)(A)'s definition of "value", applicable to § 548(a)(2)(A), does not refer to market value or worth.

Indeed, there is very little legislative history, and less Congressional guidance, as to the phrase "reasonable equivalent value" contained in 11 U.S.C. § 548(a)(2)(A). *Madrid v. Lawyers Title Insurance Corp. (In Re Madrid)* 725 F.2d 1197, 1199-1200 (9th Cir. 1984) ("*Madrid* (9th Cir.)").

The Historical and Revision Notes to § 548, "Notes of Committee on the Judiciary, Senate Report No. 95-989", pertinently state merely that

> Transfers made for less than a reasonable equivalent consideration are also vulnerable. . . .

The Court of Appeals pointed out in *In re Morris Communications NC, Inc.*, 914 F.2d 458, 466 (CA4 1990), citing other cases, that the term "reasonable equivalent value" does not mean "market value". (*See* 4 Moore & King, *Collier On Bankruptcy* (15th ed. 1992) ¶ 548.09, pp. 548-104 to 548-112).

Absent an express requirement or direction by Congress, the Bankruptcy Courts and District Courts have the duty to determine "reasonable equivalent value" based on the facts presented to them.[3]

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3. In interpreting § 548(a)(2)(A) as it applies to noncollusive purblic foreclosure sales conducted pursuant to state laws, three general lines of approach have evolved among the Court of Appeals (*See* Amicus Brief of Federal Home Loan Mortgage Corporation, p. 5, fn. 2). The *Durrett* rule, based on dicta, allows a sale to be avoided if the price paid is less than 70% of its market value. *Durrett v. Washington National Insurance Co. (In re Durrett)*, 621

(Cont'd)

Congress did not expressly restrict or prohibit those courts, in making such a determination, from applying, or harmonizing with, the foreclosure and real property laws of the States, nor did it pre-empt any relevant state laws. *California Federal Sav. & Loan Ass'n. v. Guerra,* 479 U.S. 272, 280-281, 292, 107 S. Ct. 683, 93 L. Ed. 2d 613 (1987).

Congress also did not expressly prohibit those courts, in making such a determination, from concluding, after an examination of certain factors, that an irrebuttable presumption as to value may arise.

Petitioner has failed to present any authorities or legislative history to demonstrate that Congress intended the term "reasonably equivalent value" to mean market value. As such, Petitioner's claim must be denied. *Ardestani v. I.N.S., supra; Connecticut Nat. Bank v. Germain,* __ U.S. __, 112 S. Ct. 1146, 1149-50, 117 L. Ed. 2d 391 (1992); *American Hospital Ass'n v. NLRB,* 499 U.S. __, 111 S. Ct. 1539, 1544, 1545-46, 113 L. Ed. 2d 675 (1991) — legislative history which is not directly linked to the statute under review is meaningless.

(Cont'd)
F.2d 201 (CA5 1980); *contra, Federal Deposit Insurance Corp. v. Blanton,* 918 F.2d 524, 531 fn. 7 (CA5 1990). The *Madrid* rule, followed by the Ninth Circuit below and the Sixth Circuit, creates, *after* certain facts are established, an irrebuttable presumption in favor of non-collusive, statutorily proper sales. *Lawyers Title Insurance Corp. v. Madrid* (*In re Madrid*), 21 B.R. 424 (9th Cir. BAP 1982), *aff'd on other grounds,* 725 F.2d 1197 (CA9 1984). The *Bundles* rule, asserted by Petitioner, calls for an involved case-by-case analysis after a presumption in favor of the price paid, but results in the imposition of conduct and notice beyond state statutory requirements. *Bundles v. Baker* (*In re Bundles*), 856 F.2d 815 (CA7 1988). Respondents contend that the courts hereinbelow conducted the factual investigation required by *Bundles* and other Courts of Appeals (*See* Respondent's Brief in Opposition to Amended Petition for Writ of Certiorari, pp. 8-15).

III.

CONGRESS DID NOT INTEND 11 U.S.C. § 548(a)(2) TO CHANGE PRE-CODE PRACTICE, STATE LAWS OR THE MADRID RULE.

It is well-settled that Congress does not write laws on a completely clean slate.

> The normal rule of statutory construction is that if Congress intends for legislation to change the interpretation of a judicially created concept, it makes that intent specific. *Edmonds v. Compagnie Generale Transatlantique,* 443 U.S. 256, 266-267, 99 S. Ct. 2753, 2759-60, 61 L. Ed. 2d 521 (1979). The Court has followed this rule with particular care in construing the scope of bankruptcy codifications.

Midlantic Nat. v. New Jersey Dept., 474 U.S. 494, 106 S. Ct. 755, 759, 88 L. Ed. 2d 859 (1986); *see also, United States v. Ron Pair Enterprises, Inc., supra,* 109 S. Ct. at 1032.

> Furthermore, this Court has been reluctant to accept arguments that would interpret the [Bankruptcy] Code, however vague the particular language under consideration might be, to effect a major change in pre-Code practice that is not the subject of at least some discussion in the legislative history. (Citations omitted).

Dewnsup v. Timm, __ U.S. __, 112 S. Ct. 773, 779, __ L. Ed. 2d __ (1992).

Petitioner's proposed interpretation of § 548(a)(2)(A), which would allow a statutorily valid pre-bankruptcy foreclosure to be set aside as to innocent third-party purchasers (Respondents), is contrary to pre-Code practice, and Petitioner has totally failed to demonstrate a strong Congressional intent to deviate from that practice. *Contra, see* 11 U.S.C. § 548(c) — good faith transferees will retain the interest they acquired.

Respected commentators and authorities have noted that the historical and philosophical predecessor to 11 U.S.C. § 548 was Section 67d of the Bankruptcy Act of 1898. *Madrid v. Lawyers Title Insurance Corp.* (*In re Madrid*), *supra*, 725 F.2d at 1199-1200 (CA9 1984); *In re Littleton*, 888 F.2d 90, 92 fn. 5 (CA11 1989); 4 Moore & King, *Collier On Bankruptcy* (15th ed. 1992) ¶ 548.03, p. 548-50; 4 Moore & King, *Collier On Bankruptcy* (14th ed. 1978) ¶ 67.01, pp. 15-19 — historical antecedents.

Section 67d of the Act finally used the terms "present fair equivalent value" (not "reasonably"), which had the identical meaning as the "present value" requirement of Section 70d of the Act (the predecessor to 11 U.S.C. § 549).[4] 4B Moore & King, *Collier on Bankruptcy* (14th ed. 1978) ¶ 70.68, p. 750 — Sections 67d and 70d are "parallel" statutes; *see also*, Bankruptcy Act of 1841, § 2; The English Bankruptcy Act of 1914, § 45(g) — transfers for "present fair equivalent value" were protected; *In re Chase & Sanborn Corp.*, 904 F.2d 588, 593 fn. 11 — prior Act case law is applicable to the Code.

As explained by Professor James McLaughlin at the time the Act was amended, the terms "fair equivalent value" were used instead of the word "consideration", so that technical associations with the word "consideration" would be avoided (McLaughlin, *Amendment Of The Bankruptcy Act* (1926) 40 Harv. L. Rev. 583,

4. 11 U.S.C. § 548, dealing with pre-bankruptcy transfers, is the flip side of 11 U.S.C. § 549, which deals with post-bankruptcy transfers.

614-616). In fact, the language of the Uniform Fraudulent Conveyence Act of 1919 then in existence defined "fair consideration" as a "fair equivalent". Hence, § 548's language was drafted so as to be broader than the term "consideration". (*Id.*).

Under § 67d of the Act, proper sales would not be set aside on the basis of the value of the property sold. *Security Mortgage v. Powers*, 278 U.S. 149, 156, 49 S. Ct. 84, 73 L. Ed. 236 (1928); *In re Soudan Mfg. Co.*, 113 F. 804, 808-809 (CA 7 1902) — good faith is the test; 4 Moore & King, *Collier On Bankruptcy* (14th ed. 1978) ¶ 67.17, pp. 187-188, 190-190.1, ¶ 67.02, p. 18.

Similarly, under § 10 of theBankruptcy Act of 1800 the pre-bankruptcy sale of property to bona-fide purchasers who paid "a valuable consideration" would not be invalidated or set aside.

Pre-Code practice was to not allow the set aside of validly conducted foreclosure sales if "valuable consideration" was paid by innocent purchasers. Petitioner has presented *no* evidence of Congressional intent to change this established Pre-Code practice. *In re Reinholdt*, __ F.2d __, 10 C.B.C. 1226 (D. Minn. 1984) — no such intent exists. Indeed, the lack of available legislative history leads to the conclusion that Congress never intended such a change. *Midlantic Nat. v. New Jersey Dept., supra*; *Connecticut Nat. Bank v. Germain*, *supra*, 112 S. Ct. at 1150 (concurring opinion).

In addition to a clear Pre-Code practice, the laws and decisions of the various states (at the time the Code was enacted) also precluded the setting aside of a foreclosure sale based solely on value. *Kennedy v. Dunn*, 58 Cal. 339, 340 (1881); *Johnson v. Grant*, 87 Cal. App. 402, 405 (1927); *Central Nat. Bank v. Bell*, 5 Cal. 2d 324, 328 (1936); *Stafford v. Russell*, 117 Cal. App. 2d 326, 333 (1953); *Golden v. Tomiyasu*, 79 Nev. 503, 387 P.2d 989 (1963); *Matter of Winshaw Settlor's Trust*, 758 F.2d 1136, 1139 (CA6

1985) — such laws and authorities are the "well-nigh universal rule"; R. Powell, *The Law of Real Property* (1993 ed.) § 468[6], p. 37-332-333.

Petitioner has presented no evidence of Congressional intent to change this established Pre-Code state practice and no evidence of Congressional intent to become involved in such state regulated area. As such, state laws and authorities must be allowed to stand unimpeded by the Code. *Nobelman v. American Sav. Bank*, __U.S.__, 113 S. Ct. 2106, 2110-2111, __L. Ed. 2d __ (1993).

Indeed, it is indisputable that Congress has regularly and knowingly not (in almost 15 years) taken a position, nor defined any guidelines, in view of the assorted decisions regarding "reasonable equivalent value". *In Re Ehring*, 91 B.R. 897, 901 (9th Cir. BAP 1988), *aff'd*, 900 F.2d 184, 189 (1990); *In Re Verna*, 58 B.R. 246, 250, 251 (Bk. C.D. Cal. 1986); *In Re Kachanizadeh*. 108 B.R. 734, 736 (Bk. C.D. Cal. 1989).

In addition, despite obviously being aware of it, Congress has never drafted legislation nor created any other prohibition or proclamation to overrule, negate, restrict or weaken the authority and reasoning of the 1982 decision in *Madrid* (9th Cir. BAP). (*Id.*) Yet, since that decision in 1982 (over 11 years ago), Congress has amended the Bankruptcy Code five times (in 1984, 1986, 1988, 1990 and 1992). By failing to make revisions in the Bankruptcy Code to overrule *Madrid* (9th Cir. BAP), Congress has tacitly approved that decision.[5] *Lorillard v. Pons*, 434 U.S. 575, 580, 90 S.

5. Congress' seeming partial nolens volens overruling of *Madrid* (9th Cir.) through the 1984 Amendments, relating to 11 U.S.C. § 101, did not affect *Madrid* (BAP) as it was based on different reasoning than *Madrid* (9th). (*Dewsnup v. Timm*, __U.S.__, 1125 S. Ct. 773, 779, __L. Ed. 2d__ (1992); *Muniz v. Hoffman*, 422 U.S. 454, 472, 95 S. Ct. 2178, 45 L. Ed. 2d 319 (1975); W. Conant, *Beyond Madrid: Resolving The Conflict Within The Ninth Circuit* *(Cont'd)*

Ct. 866, 55 L. Ed. 2d 40 (1978); *In Re Execuair Corp.*, 125 B.R. 600, 602-03, 604 (Bk. C.D. Cal. 1991); *see also Dewsnup v. Timm*, *supra*.

If any Congressional intent exists with respect to determining "reasonable equivalent value" under 11 U.S.C. § 548(a)(2)(A) it is that Congress has not intended to overrule *Madrid* (9th BAP) or any other decision. In effect, Congress' intent is obviously to leave such determinations to the various Courts of Appeal, which should apply state foreclosure laws, at least in part. It should also be clear that Congress has not prohibited consideration of, nor pre-empted, the laws of the states as to foreclosure or real property in any determination as to "reasonable equivalent value".

This Supreme Court should not substitute or impose any other intent as to the making of such determinations. Petitioner's claim must be denied.

IV.

THE NINTH CIRCUIT'S DECISION BELOW IS NOT CONTRARY TO THE INTENT OR PURPOSES OF THE BANKRUPTCY CODE.

Petitioner and amici supporting it contend that the Ninth Circuit's decision below is contrary to the purposes of the Bankruptcy Code. Nothing could be further from the truth.

At a minimum, the Ninth Circuit reached a decision which promoted harmony with state laws and authorities, and which allowed state laws and authorities to remain valid. Such a result is

(Cont'd)
Regarding § 548(a)(2)(A) *And Nonjudicial Foreclosure Sales*, 18 Cal. Bankr. J. 221, 240, 241 (1990).)

always preferred. *Cf. Rake v. Wade*, ___U.S.___, 113 S. Ct. 2187, 2192, ___L. Ed. 2d___ (1993); *see* Point IV, *infra*.

Allowing state foreclosure and property laws to apply[6], or presumptions to be reached by courts as to "value", does not interfere with the overall purposes of the Bankruptcy Code and Congress.

The Bankruptcy Code indisputably provides that a creditor's right to foreclosure is not threatened or terminated by a bankruptcy case, and is unaffected by a discharge (*Johnson v. Home State Bank*, ___U.S.___, 11 S. Ct. 2150, 2153-54 (1991)). In particular, the avoidance powers set forth in the Bankruptcy Code are intended to assure an equitable distribution among unsecured creditors, which surely does not mean Congress intended to let the interests of unsecured creditors to override the rights of trust deed holders or good faith purchasers. *Matter of Winshaw Settlor's Trust, supra*, 758 F.2d at 1139 fn. 4.

This Court has specifically recognized that the justifications for application of state laws in bankruptcy cases include the protection of secured interests and mortgagees because the rights

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6. Generally, congress has not attempted, within the Bankruptcy Code, to enact, or pre-empt the states' laws regarding foreclosure, mortgages or real property (*Barnhill v. Johnson, supra*, 112 S. Ct. at 1389; *Dewsnup v. Timm, supra*, 112 S. Ct. at 778-779; *Johnson v. Home State Bank, supra*, 111 S. Ct. at 2153; *Farrey v. Sanderfoot*, 500 U.S. ___, 111 S. Ct. 1825, 1829, ___ L. Ed. 2d ___ (1991); *Grogan v. Garner*, 498 U.S. 279, 657, 111 S. Ct. 654, 657, 112 L. Ed. 2d 755 (1991); *Butner v. United States*, 440 U.S. 48, 54-56, 99 S. Ct. 914, 59 L. Ed. 2d 136 (1978) — unless some federal interest requires a different result, state property law should be applied in bankruptcy; *In Re Rigden*, 795 F.2d 727, 736 fn. 1 (9th Cir. 1986) — state laws determine many rights in bankruptcy cases.) Pertinent to Respondents herein and in accord with a majority of state foreclosure laws, the bankruptcy laws have always been intended to protect bona fide purchasers. *See* Point III, *supra*.

of secured creditors were "bargained for" by the debtor and are protected by the Code. *Nobleman v. American Sav. Bank, supra*, 113 S. Ct. at 2110-2111; *Rake v. Wade, supra*; *see also*, 11 U.S.C. §§ 361, 362(d), 363(b)(1), 506, 545(2), 546(b), 549(c), 552(b), 724(b)(1), 725, 1102(a)(2), 1110(a), 1111(b)(1), 1123, 1129(b)(2)(A), 1322(b)(2), and 1325(a)(5).

The only potential asset lost at a foreclosure sale is the equity, if any, in the property sold. Such equity, however, accrues to the benefit of secured creditors, not debtors or unsecured creditors. *Dewsnup v. Timm, supra*, 112 S. Ct. at 778.

Herein, there was no lost equity. The property was encumbered by a senior trust deed of $421,815.72 and a junior trust deed of at least $200,000, totalling $621,815.72. Respondents purchased the property for $433,000, demonstrating a negative equity of [$-188,815.72]. Indeed, as the junior trust deed was extinguished by the foreclosure sale, Petitioner received a significant benefit. *In Re Littleton, supra*, 888 F.2d at 90, 93-94 (CA11 1989).

State foreclosure laws, which do not allow foreclosure sales to be set aside solely on the basis of an inadequate price (*see* Point III, *supra*), do not interfere or conflict with Congress' intent or the goals for bankruptcy cases. Such laws require determinations that: the foreclosure sale was conducted pursuant to statutory procedures; full noticing and competitive bidding occurred; the debt owed on the trust deed was paid; no fraud or collusion was present; no extraordinary circumstances existed; among other things. *Central Nat. Bank v. Bell, supra*, 5 Cal. 2d at 328.

Such determinations are implicit in 11 U.S.C. § 548(a)(2)(A), and are recommended by the *Bundles* approach. As noted in Respondent's Brief in Opposition, pp. 8-15, such determinations were made by the Bankruptcy Court below, based on a multitude of documents and evidence presented to it.

Hereinbelow, the Bankruptcy Court, in matters concerning Petitioner's complaint and the foreclosure sale, held evidentiary hearings on Respondents' Motion to Dismiss, Respondents' Motion For Relief From Automatic Stay and on Imperial's Motions For Summary Judgment, in addition to numerous adversary and case hearings (J.A. pp. 63-236; 298-299; 300-315; 1-5; 23-25; 26-32) The determination by the Bankruptcy Court below considered all the pertinent factors which § 548 requires, and *Bundles* said, should be examined.

The single most important non-price factor as stated by *Bundles* was compliance with state foreclosure sale requirements. (856 F.2d at 825) Hereinbelow, the Bankruptcy Court was apprised by Petitioner that it could not demonstrate that any California requirements were not fully complied with. Upon receiving competent evidence, the Bankruptcy Court also reached a specific judgment that the foreclosure sale was regularly and properly conducted. *See Madrid,* 21 B.R. at 426-427 (9th Cir. BAP) — compliance with state laws is, in accord with bankruptcy purposes, "a safeguard against the evils of private transfers to relatives or favorites."

As to the determination of a fair appraisal (856 F.2d at 824), California foreclosure statutes do not contain a requirement for such a document. *See* Calif. Civil Code § 2824 *et seq.* ("the California foreclosure statutes"); §§ 2924f, 2924g, 2924h — no appraisal is required for a foreclosure (trustee's) sales)). California nonjudicial foreclosure sales are sales which are governed by the highest price received at a public sale. *See* Calif. Civil Codes §§ 2924h (c) — property is sold based on "the last and highest bid". As such, the appraisal factor is of no consequence.

In any event, the Bankruptcy Court herein was presented with Petitioner's bankruptcy Schedules, adversary pleadings and self-serving declarations as to the property's alleged value (J.A., pp.

38-40; 59-60;2). Apparently Petitioner submitted no appraisals.

As to determining advertising for the sale (856 F.2d at 824)[7], California foreclosure statutes contain strict comprehensive requirements for noticing, posting and advertising. *See* Calif. Civil Code §§ 2924, 2924b, 2924c, 2924f — publication in a "newspaper of general circulation" once a week for 20 days; *see also,* R. Powell, *The Law of Real Property* (1993 ed.), § 466, p. 37-316 — all such prerequisites for sale are established by local law. As such, the only noticing and advertising required is that contained in the foreclosure statutes. *U.S. Cold Storage v. Great Western Sav. & Loan Ass'n,* 165 Cal. App. 3d 1214, 1229-30 (1985); *Strutt v. Ontario Sav. & Loan,* 28 Cal. App. 3d 866, 877 (1972). The Bankruptcy Court was presented with evidence of compliance with the California foreclosure statutes, which Petitioner could not refute.

As to determining whether competitive bidding was encouraged (856 F.2d at 824), the Bankruptcy Court was presented with evidence of obvious overbidding. Respondents' highest bid price was over $11,780 higher than the amount actually due on Imperial's foreclosed-upon deed of trust. That $11,780 surplus was made available to the holders of a $200,000 deed of trust in a junior position to Imperial's deed of trust. *See In re Littleton, supra,* 888 F.2d at 93-94 — reasonable equivalent value has clearly been paid when junior liens are also extinguished by the foreclosure sale.

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7. It is with this factor in particular, but also possibly others (*e.g.*, appraisal requirement), where other courts have interpreted *Bundles* (and particularly its use of the word "widely", 856 F.2d at 824) to require foreclosure sale actions and conduct to *exceed* the precise mandates under the comprehensive foreclosure laws of the states (*See In Re Lindsay* 95 B.R. 983, 991 (Bk. S. D. Cal. 1989); *see also In Re Kachanizadeh,* 108 B. R. 734, 738 — *Lindsay* violated *stare decisis* and was an improper decision). Imposing additional sale requirements will thus create a conflict, and result in tension, with the specific state laws of foreclosure.

In addition, the California foreclosure statutes require and encourage competitive bidding. Calif. Civil Code § 2924h; *see* § 2924h(g) — the fixing or restraining of bidding can result in fines and imprisonment; *Lupertino v. Carbajal*, 35 Cal. App. 3d 742, 746-47 (1973); R. Powell, *The Law of Real Property* (1993 ed.), § 439, p.137-14.

Thus, at several stages and evidentiary hearings, the Bankruptcy Court below was presented with ample evidence as to all the § 548 and *Bundles'* factors, which sufficiently demonstrated that a reasonably equivalent value had been paid by Respondents at the foreclosure sale. The examination of all relevant circumstances was made by the Bankruptcy Court herein. Therefore, as stated by *Bundles*, "we must accord [the Bankruptcy Court's determination] great deference." (856 F.2d at 825).

While the Seventh Circuit might disagree with the wording of the Ninth Circuit's opinion below, it could not disagree with the result herein. That result, of upholding the foreclosure sale, was derived herein from the same type of examination and analysis called for in *Bundles*.

Indeed, the Ninth Circuit's decision below, and the creation of any presumption, expressly requires findings as to: the lack of collusion or fraud; the propriety of conduct at the sale; compliance with State foreclosure requirements (which include noticing and bidding); and the price paid. These findings will, in addition, necessarily be made in light of: the debtor's bankruptcy pleadings (setting forth, *inter alia*, assets, debts and asserted property values); the debtor's alleged damages or loss of equity (as required by Rule 7009, Federal Rules of Bankruptcy Procedure and Rule 9 (g), F.R.C.P. — claims for damages must be specifically stated); and any other evidence submitted by the parties. Only *after* making a determination that the required elements do exist can a court conclude, according to the Ninth Circuit, that there is a presumption in favor of the price paid at the foreclosure sale.

Inasmuch as the determinations required by state foreclosure laws, and the determinations required by the Ninth Circuit's decision below, involve various factors which are implicitly to be determined pursuant to 11 U.S.C. § 548(a)(2)(A), and do not interfere or directly conflict with the Bankruptcy Code, they are permissible and not pre-empted.

V.

THE BANKRUPTCY COURT DID NOT ERR IN DISMISSING PETITIONER'S COMPLAINT.

Petitioner contends that its complaint should not have been dismissed on the basis that it failed to state a claim for relief.

The *Conley* case cited by Petitioner (Petitioner's Brief, p. 25) is not applicable. It involved a motion for judgment on the pleadings; herein, Respondents filed a motion to dismiss.

Petitioner's citation to *Kelson v. Springfield*, 767 F.2d 651 (CA9 1988) is correct but that decision is contrary to Petitioner's position. As pointed out in *Kelson*, the issue on a motion to dismiss is one of law — assuming the alleged facts are true is there a legal basis for the stated claim?

Hereinbelow, there clearly was no such legal basis for Petitioner's complaint. As noted by the Bankruptcy Court, *Madrid* (BAP) was still the law in the Ninth Circuit. *See* Appendix to Petitioner's Amended Petition, pp. 28-32; *see also In re BFP*, 974 F.2d 1144, 1148 (CA9 1992). The Bankruptcy Court was bound to follow the *Madrid* (BAP) decision. *Bank of Maui v. Estate Analysis, Inc.*, 904 F.2d 470, 471-472 (CA9 1990); *In re Kachanizadeh, supra*, 108 B.R. at 738 (Bk. C.D. Cal. 1989). Any contrary ruling would have violated the doctrine of *stare decisis*.

Based on the facts as admitted by Petitioner to the Bankruptcy

Court, there was no legal basis upon which Petitioner could proceed. Petitioner had informed the court that it could not contest compliance with state laws or show collusion or fraud.

The Bankruptcy Court applied the proper standard of review and did not err in dismissing Petitioner's complaint as to Respondents. Indeed, a contrary decision would have violated established principles and authorities, and would have been in error.

VI.

THE NINTH CIRCUIT'S DECISION CREATED HARMONY BETWEEN EXISTING STATE SUBSTANTIVE LAWS AND FEDERAL BANKRUPTCY LAW, AND WAS CORRECT.

As noted herein above (Point IV, *supra*), the Bankruptcy Court made the proper evidentiary determinations implicitly required by the Bankruptcy Code. With the correct result at hand, the Ninth Circuit attempted in its decision below to avoid conflicts with State law.[8][9] It concluded that:

8. Herein, it is well-settled under the laws of California, and other states, that a foreclosure sale may not be set aside based solely on the inadequacy of price absent the showing of some other irregularity. *See* Point III, *supra*. In addition, and particularly pertinent as to Respondents, California foreclosure statutes expressly create a "conclusive presumption" in favor of bona fide purchasers at foreclosure sales. Calif. Civil Code § 2924; *Wolf v. Lipsy*, 163 Cal. App. 3d 633, 639 (1985) — this conclusive presumption is irrebuttable; *Napue v. Gor-Mey West, Inc.*, 175 Cal. App. 3d 608, 613 (1985); *Karrell v. First Thrift of Los Angeles*, 104 Cal. App. 2d 536, 539 (1951). Significantly, California law provides that if a sale is set aside, the foreclosing beneficiary/trustee is liable to repay the price paid plus interest. *Little v. CFS Service Corp.*, 188 Cal. App. 3d 1354 (1987).

9. The Ninth Circuit's decision below was also in harmony with other (Cont'd)

> [B]y following the Madrid formulation we are able to give a reasonable meaning to § 548 without unduly upsetting local real estate markets or state law. Unlike the *Bundles* court, we see the issue as *both* one of statutory interpretation *and* the growing tension between preemption and the requirements of a vigorous federal system . . . Thus, by interpreting § 548 in accordance with the Madrid formulation, we are able to balance bankruptcy policy and comity concerns.[6]"

(974 F.2d at 1149)

Other Courts of Appeal have agreed:

> . . . The better view is that reasonable equivalence for the purposes of a foreclosure sale under § 548(a)(2)(A) should be consonant with the state law of fraudulent conveyances . . . No support for this drastic upset of state law and procedures is found in the Bankruptcy Code.

Matter of Winshaw Settlor's Trust, supra, 758 F.2d at 1139-40; *see also Gottlieb v. McArdle*, 580 F. Supp. 1523, 1525 — under federal law, a foreclosure sale should be set aside only if the price paid shocks our conscience).

(Cont'd)
decisions regarding applying state law, and decisions interpreting different avoidance sections of the Bankruptcy Code, which decisions also authorized regularly conducted foreclosure sales to stand (*See In Re Ehring* 91 B.R. 897, 900 (9th Cir. BAP), *aff'd*, 900 F.2d 184 (1990) —11 U.S.C. § 547; *In Re Walker*, 861 F.2d 597 (9th Cir. 1988) — 11 U.S.C. § 549(c), if the purchasers record first).

> [I]t is important to interpret the two [bankruptcy law and state law] statutes in a way that minimizes such conflicts and harmonizes the policies that underlie them.

Kapela v. Newman, 649 F.2d 887, 890-91 (CA1 1981); *see also County of Yakima v. Yakima Indian Nation*, ___U.S.___, 112 S. Ct. 683, 692, 116 L. Ed. 2d 687 — courts must harmonize statutes on the same topic so that each is left effective; *Fed'l Trade Comm. v. Bunte Bros. Inc.*, 312 U.S. 349, 61 S. Ct. 580, 582, 85 L. Ed. 881 (1941); *Chicago & N.W.R. Co. v. Lindell*, 231 U.S. 14, 18, 50 S. Ct. 200, 201, 74 L. Ed. 670 (1930) — due regard must be given for a proper adjustment of local and national interests and laws.

The Ninth Circuit's decision below does just that, and in a way which does not interfere or conflict with Bankruptcy Code purposes or Congressional intent. The Court of Appeals was faced with reconciling a simple bankruptcy statute with a comprehensive system of state foreclosure laws.[10]

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10. The Ninth Circuit also understood that a restrictive interpretation could result in undesirable consequences both on a bankruptcy and state level. Indeed, these consequences would be contrary to any price-maximizing objective of the Bankruptcy Code. "It makes little sense to interpret § 548(a)(2)(A) in a way that will likely discourage healthy foreclosure bidding." (974 F.2d at 1148-1149) The chilling effect which could result from a pre-emptive interpretation of 11 U.S.C. 548(a)(2)(A) is obvious and has been widely discussed. *Matter of Grissom*, 955 F.2d 1440, 1446; *Matter of Winshaw Settlor's Trust, supra*, 758 F.2d at 1139; *Abramson v. Lakewood Bank & Trust Co.*, 647 F.2d 547, 550 (dissent); *In Re Verna, supra*, 58 B.R. at 252 — a rule of certainty is necessary to encourage bidders, maximize amounts paid and create a market for sales; S. Ehrlich, *Avoidance of Foreclosure Sales as Fraudulent Conveyances: Accommodating State and Federal Objections*, 71 Va. L. Re. 933, 963-64, 980 (1985). Indeed, this Court should interpret federal bankruptcy laws so as to encourage the flow of capital and lending. *Nobelman v. American Sav. Bank, supra*, 113 S. Ct. at 2112 (concurring opinion).

As the California Supreme Court explained in *I.E. Associates v. Safeco Title Ins. Co.*, 39 Cal. 3d 281, 288:

> There are, moreover, persuasive policy reasons which militate against a judicial expansion of those [State statutory] duties. The nonjudicial foreclosure statutes — an alternative to judicial foreclosure — reflect a careful crafted balance of the interests of the beneficiary, trustors and trustees . . . In taking all these concerns into account, the statutes strike an overall balance favoring the protection of trustors (Citations omitted.).

See also, Garfinkle v. Superior Court, 21 Cal. 3d 268, 278 (1978); *Smith v. Allen*, 68 Cal. 2d 93, 96 (1968); *Pacific Scene, Inc. v. Penasquitos, Inc.*, 46 Cal. 3d 407, 411 (1988) — such comprehensive legislation indicates a clear legislative intent that the statutory system shall be totally controlling in the area legislated.

As this Supreme Court has made clear

> Uniform treatment of property interests by both state and federal courts within a State serves to reduce uncertainty, to discourage forum shopping, and to prevent a party from receiving "a windfall merely by reason of that happenstance of bankruptcy." *Lewis v. Manufacturers National Bank*, 364 U.S. 603, 609. The justifications for application of state law are not limited to ownership interests; they apply with equal force to security interests, including the interest of a mortgagee . . .

Butner v. United States, 440 U.S. at 55.

VII.

PETITIONER INCORRECTLY ASSERTS THAT NOTICE DEFECTS WOULD JUSTIFY SETTING ASIDE THE FORECLOSURE SALE.

Petitioner asserts, incorrectly, that the foreclosure sale can be set aside because of the alleged defects in giving notice of the sale (Petitioner's Brief, p. 47).

Petitioner misstates the law.

The only notice required is that called for in California's foreclosure statutes. *U.S. Cold Storage, supra,* 165 Cal. App. 3d at 1229-30. Indeed, Petitioner admitted to the Bankruptcy Court that all California statutory requirements had been complied with *(See* Appendix to Petitioner's Amended Petition, pp. 28-32).

More importantly, California law specifically provides that third party bona fide purchasers obtain a conclusive presumption that all noticing and other statutory requirements have been complied with. Calif. Civil Code § 2924; *Wolf v. Lipsy, supra,* 163 Cal. App. 3d at 639. Accordingly, it is well-settled that a foreclosure sale may not be set aside, as to third-party bona fide purchasers like Respondents, due to any defect in notice. *Napue v. Gor-Mey West, Inc., supra,* 175 Cal. App. 3d at 613. *See* 11 U.S.C. § 548(c).

Petitioner's assertion to the contrary is false.

CONCLUSION

The Bankruptcy Court below made the determinations, and reviewed all relevant factors, as required by § 548 and most Courts of Appeals.

The application of state foreclosure law, or the reaching of an irrebuttable presumption after an evidentiary determination, are not prohibited by, or in conflict with, Bankruptcy Code purposes or Congressional intent.

Congress has never expressed any intent that § 548 was to change pre-Code practice or existing state laws, which allowed properly conducted foreclosure sales for value to remain valid. Without a clear expression of such an intention, this Court should not deviate from those practices or laws.

Congress has tacitly approved of, and has never overruled or disapproved of, the opinion in *Madrid* (9th Cir. BAP), which was a basis for the Ninth Circuit's decision below. Indeed, Congress' intent in light of almost 15 years of decisions, is to leave a determination under 11 U.S.C. § 548(a)(2)(A) to the various Courts of Appeals, subject to state foreclosure laws.

The Ninth Circuit's decision promoted harmony with complex state laws, encouraged bidding at sales, created stability and finality, enhanced potential recoveries by debtors and creditors, and promoted an active market place for real property which is essential to the well-being of this country.

If this Court were to take the position asserted by Petitioner it would force tens of thousands of lenders, investors, or foreclosure trustees to set up reserves for repayment to successful third-party purchasers in order to deal with potential sale set-asides which might occur years in the future. Such a result would be expensive,

cumbersome and disastrous to the real estate, foreclosure and lending industries.

The Ninth Circuit's decision was not erroneous and must be permitted to stand.

For these reasons, and other reasons as may be apparent herein, this Supreme Court should deny Petitioner's requests.

Respectfully submitted,

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